No. 7307.

In the

United States

Circuit Court of Appeals,

FOR THE NINTH CIRCUIT.

Stanley S. Anderson,
Petitioner,

vs.

Commissioner of Internal Revenue,
Respondent.

PETITIONER'S REPLY BRIEF.

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REPLY BRIEF.

The legal points and authorities involved in this proceeding have been covered fully in our opening brief and apparently are not controverted by the respondent. However, the brief for respondent is so at variance with our understanding of the Board's findings of facts and basis of decision that further analysis and comments appear advisable.

1. The Real Basis of the Board's Decision.

Respondent contends that the only issue before the Board was one of fact, whether there was any agreement between petitioner and his wife that she should have a separate property interest, and concludes that the Board

found *as a matter of fact* that there was no such agreement. This, we submit, is incorrect.

As set forth in our opening brief, the Board found expressly that there was such an agreement between the petitioner and his wife, as evidenced by the following quotations from the Board's findings of fact:

> "* * * it being agreed between them, however, that the commission should belong one-half to each." [Tr. 31.]
>
> "It was specifically agreed that she would share equally with the petitioner the yearly salary and the profits, if any." [Tr. 32.]
>
> "* * * and was deposited in a joint bank account for himself and his wife." [Tr. 32.]
>
> "Soon after this transaction the petitioner's wife asked him to prepare a written memorandum defining his and her respective rights in the investment" (referring to the letter of Sept. 5, 1932). [Tr. 33.]
>
> "In the books of the new company separate accounts were set up for the petitioner and his wife, showing them owners of separate equal interests." [Tr. 34.]
>
> "From time to time the petitioner and his wife made other investments with their joint earnings and profits, with the understanding and agreement that they were equal owners therein and that each was entitled to receive one-half of the profits and was liable for one-half of the losses." [Tr. 34.]
>
> "Edwin Janss, president of the Janss Investment Co., and Charles H. Christie both understood that Marguerite S. Anderson and the petitioner owned equal interests in their investment." [Tr. 35.]

"Near the end of 1926 the petitioner inquired if his wife's share of the earnings from the 'Young's Building' were being credited to her and, being informed that they were not, had the auditor open an account entitled 'Joint M. S. Anderson' in which was set up the Young's Building at a valuation of $202,788. Also, at about that time another account was opened as of January 1, 1926 (should be January 1, 1925—see Exhibit No. 42), entitled 'Janss Inv. Co. Joint M. S. Anderson'. Also, at about that time, another account was set up for 'Marguerite S. Anderson'." [Tr. 35.]

"The petitioner informed the auditor in 1920 that one-half of the profits from the hotel belong to his wife separately * * *." [Tr. 37.]

From the above express findings it is clear that the Board thought, and so held, that there was a definite agreement (or agreements) between petitioner and his wife that she should have an equal half interest in the various properties as her separate property. The real basis for the Board's adverse decision is shown in the concluding paragraphs of the opinion, as follows:

"Aside from the *presumption of law* which, as we have said, operates in favor of the respondent's contention that the income in question was community income, the very nature of the question here calls for the *strictest proof* on the petitioner's part. Where, as in the instant case, the written records and the acts of the husband and wife for a number of years indicate that, either ill-advisedly or without knowing the result upon their tax liability, they have submitted to the community property law of their state, they should not be permitted to avoid the legal conse-

quences of that rule *merely upon their own testimony* that they had previously entered into an *oral agreement between themselves* by which their property rights must be determined upon some other than the community property basis. We cannot escape the conviction that this is the *tenor of the cases* in which the courts have considered this question.

"Upon the evidence before us, we are not convinced of the existence of any *valid enforceable* agreement between the petitioner and his wife, prior to the written agreement executed on June 8, 1932, that their income and property should be owned by them otherwise than 'on an equal footing' as in Blair v. Roth, *supra*. We are therefore of the opinion that the petitioner has not overcome the presumption of the correctness of the respondent's determination that the income in question for the years 1924 and 1925 was community income taxable to the petitioner." [Tr. 46-47.] (Italics ours.)

From the above it seems clear that the Board recognized the existence of an oral agreement, but felt that it was legally unenforceable and could not prevail as against the presumption in favor of community property. The Board's decision was based upon the following clear errors of law:

(1) The presumption as to community property was not evidence and had no probative force. (See pp. 38-42 of opening brief.)

(2) An oral agreement between a husband and wife is sufficient in California to transmute into separate property what would otherwise be community property. (See pp. 22-38 of opening brief.)

(3) The "tenor of the cases" cited by the Board did not require its decision in this case. (See pp. 43-47 of opening brief.)

Furthermore, the Board erred in assuming, contrary to its own express findings, that the petitioner and his wife were relying "merely upon their own testimony that they had previously entered into an oral agreement". While such testimony would be sufficient under California law to establish a separate property status (see pp. 26-33 of opening brief), the record clearly discloses a vast volume of corroborative testimony of disinterested witnesses as well as documentary evidence, such as the following:

1. The testimony of Dr. Edwin Janss, manager of the real estate syndicates. [Tr. 69-77.]

2. The testimony of Charles H. Christie, another member of the syndicates. [Tr. 82-83.]

3. The testimony of M. R. Moulthrop, Esq., attorney for petitioner and his mother. [Tr. 85-88.]

4. The testimony of J. H. Slattery, father of petitioner's wife. [Tr. 107-108.]

5. The testimony of E. P. Adams, certified public accountant. [Tr. 115-118.]

6. The letter from petitioner to his wife, dated September 5, 1923. [Pet. Exh. Nos. 18 and 26.]

7. Numerous deeds, notes, mortgages and other documents executed by Mrs. Anderson. [Pet. Exh. Nos. 12-16, 19-20, 27-39.]

8. The deed to 37 acres of the syndicate property, from Janss Investment Co. to "Stanley S. Anderson

and Marguerite S. Anderson", executed August 16, 1926, and duly recorded. [Pet. Exh. No. 16.]

9. The various entries and accounts in the records of petitioner. [Pet. Exh. Nos. 41, 42, 43.]

10. The separate returns filed for the taxable years in question. [Tr. 38.]

11. The separate accounts set up on the new books of the Janss Investment Corporation, on January 1, 1929. [Tr. 34.]

12. The agreement dated June 8, 1932. [Tr. 36-37.]

Clearly, petitioner's case did not rest "merely upon" the testimony of himself and his wife that they had an oral agreement. It is supported without contradiction by the testimony of five disinterested witnesses as well as considerable documentary evidence. The Board clearly erred in ignoring this evidence, as set forth in its own findings of facts.

2. Findings of Fact by the Board.

It is the duty of the Board to make "all reasonably requisite findings of fact". (*Brampton Woolen Co. v. Commissioner,* 45 F. (2d) 327.) It is essential that findings of fact shall be clear, intelligible, definite, certain and unequivocal. They shall not be vague or evasive. (64 *C. J.,* 1247, 1248.)

Consideration of the Board's "findings of fact" alone would lead clearly to the conclusion that there was a

definite separate property agreement between petitioner and his wife. Respondent seeks to support the contradictory decision of the Board by alleged additional findings in the opinion. Careful study of the opinion discloses that there are no additional clear or definite findings of *facts* to be found there, but merely conclusions of law or mixed statements of law and fact. Surely such ambiguous and indefinite conclusions cannot outweigh the clear and express facts set forth in the formal findings.

A finding of fact designed to negative an affirmative allegation of the petition, which is equivocal or evasive, is equivalent to a negative pregnant in pleading and serves as an admission of the fact alleged.

> "A finding in the form of a negative pregnant, attempting to negative an affirmative allegation, implies the truth of the allegation."
>
> *Wiles v. Hammer,* 66 Cal. App. 538, 540.

To the same effect see:

Tormey v. Anderson-Cottonwood Irrigation District, 53 Cal. App. 559, 562;

Auerbach v. Healy, 174 Cal. 60, 65;

Southern Pacific R. R. Co. v. Dufour, 95 Cal. 615, 618-619;

State v. Box (Texas), 78 S. W. 982, 984;

Bartholomew v. Fayette Irr. Co. (Utah), 86 P. 481, 483.

For example, the finding in the Board's opinion (if it can be deemed a finding), that "We are not convinced

of the existence of any *valid enforceable* agreement between the petitioner and his wife * * *" [Tr. 47], if considered by itself alone, would amount to nothing more than a negative pregnant admitting the existence of the agreement but denying that it was valid or enforceable. This, of course, is merely a conclusion of law that a parol agreement between husband and wife is ineffective to transmute their community property into separate property. This is conclusively confirmed when we refer to the Board's formal findings and note that the Board there expressly found that the agreements were made as contended by petitioner. (See pp. 2-3, 4-5, above.)

There is no escape from the conclusion that the Board found all of the *facts* in favor of petitioner's contentions. It decided against the petitioner solely upon the basis of a *conclusion of law,* to-wit, that a parol agreement between husband and wife, unaccompanied by the execution and delivery of instruments of conveyance, is ineffective to transmute their community property into separate property. This conclusion of law is utterly erroneous, as is demonstrated by the California authorities cited in our opening brief.

In this connection it should be noted that three members of the Board joined in a dissenting opinion on the ground that there was an effective contract between petitioner and his wife "under which each acquired and held, as tenants in common, a separate one-half interest in these properties and, consequently, the income therefrom should be taxed, one-half separately to each." [Tr. 48.]

3. Beverly Hills Lots.

Petitioner pointed out in his opening brief (pp. 48-49) that of the purchase price of these lots, to-wit, $13,200.00, the sum of $3,200.00 was paid from what was admittedly Mrs. Anderson's separate property, being derived by gift from her father. This being so, she was during the years in question the owner of at least 32/132 of this property in the absence of an effective agreement to the contrary. Counsel for respondent deny this (pp. 20-21), asserting that if the improvements on these lots were made from community funds, the wife's fractional interest therein would be decreased in proportion to the amount of community funds expended in the improvements. Counsel cite no authority in support of their assertion, nor do they attempt to distinguish the California cases to the contrary which were cited in our opening brief (p. 49).

Their unsupported assertion is directly contrary to the settled law in California, which governs this case, that where improvements are made with community funds upon real property which is the separate property of one of the spouses, the title to the improvements remains with the title to the land in the absence of an agreement to the contrary.

For example, in *Dunn v. Mullan,* 211 Cal. 583, 589 (1931), the wife was the owner of an undivided one-half interest in certain unimproved real property as her separate property, the other one-half interest therein being owned by the husband as community property. Extensive

improvements were made thereon out of community funds and the court held squarely that the wife continued to be the owner, as her separate property, of a one-half interest in both the land and the improvements. The court said:

> "This is necessarily so for it is the general rule that improvements made during marriage on the separate property of either husband or wife, although with community funds, belong to the spouse owning the separate property."

So, likewise, in *Smith v. Smith,* 47 Cal. App. 650,653-4, the court held that

> "The expenditures by a husband of either his separate funds or the common funds of himself and wife in improving his wife's separate property does not operate to change the title."

Among the other California decisions to the same effect are the following:

Potter v. Smith, 48 Cal. App. 162, 166;
Estate of Barreiro, 86 Cal. App. 764, 766;
Provost v. Provost, 102 Cal. App. 775, 779;
Spreng v. Spreng, 119 Cal. App. 155, 159;
Peck v. Brummagim, 31 Cal. 440, 448-9;
Seligman v. Seligman, 85 Cal. App. 683, 688-9.

It follows inevitably that the Board's decision herein is erroneous under any and every tenable theory of the law. Of course, we are not contending that petitioner's wife is the owner of merely 32/132nds of the Beverly Hills property. Our contention is that she was the owner

of an undivided one-half thereof as her separate property. The Board expressly found that it was agreed between her and her husband that the real estate commission of $10,000.00, which went into the purchase of this property, "should belong one-half to each" [Tr. 31]. This being so, it necessarily follows that she contributed $8,200.00 of the $13,200.00 purchase price of these lots. Therefore, in the absence of an agreement to the contrary, she would now be the owner of 82/132nds of that property, together with all improvements thereon and the income therefrom. The fact is, however, that she is the owner of an undivided one-half interest therein as her separate property and petitioner is the owner of the other one-half interest therein. The spouses agreed to this, and their agreement to this effect is proved by the uncontradicted testimony herein. [Tr. 91, 92, 108, 109.]

4. Earnings From Services as Distinguished From Income From Properties.

On page 19 of their brief, counsel make the following statements:

> "Petitioner concedes for the purpose of this appeal that the earnings of petitioner and his wife in prior years were properly taxable to the husband as community income for the taxable years in which received. In this there appears to be an inconsistency in view of the statements that agreements existed creating separate properties in the income earned by each. * * *"

The legal situation, under the present authorities is as follows:

(1) In *Lucas v. Earl,* 281 U. S. 111, the Supreme Court held that an antecedent agreement was ineffective to prevent the taxation to the husband of fees and salaries earned by him, though recognizing that immediately thereafter the funds would be vested, under the agreement, with the status of joint or separate property. This decision has been followed consistently by this court in such cases as *Blair v. Roth,* 22 F. (2d) 932; *Belcher v. Lucas,* 39 F. (2d) 74, and *Pedder v. Commissioner,* 60 F. (2d) 866.

(2) However, the Board of Tax Appeals has held to be effective antecedent agreements that the earnings of a particular spouse shall be his or her separate property and taxable accordingly, instead of being taxed as community property. Thus, in *Howard C. Hickman,* 27 B. T. A. 807 (now pending before this Court), the Board held that under an agreement that the compensation received by a California wife for her personal services should be her separate income and separate property, such compensation may not be treated as community income and taxed to the husband. Likewise, in *Helen E. Grant,* January 16, 1934, the Board held that where a husband and wife domiciled in California enter into a valid agreement that the earnings and salary of the husband after the date thereof shall be the separate income and property of the husband, no part of such earnings and salary is taxable to the wife.

In the present case the earnings of petitioner and his wife were received on account of their joint services and

it was agreed in advance that one-half of such compensation should be the separate property of each of them. Under the above decisions of the Board, it would be arguable that such income was taxable one-half to each of them, provided that they had elected to file separate returns.

However, the compensation for their services was received during taxable years prior to those here in question and, due to the advice of the auditor who prepared their returns [Tr. 117-118], joint returns were filed. For the years 1924 and 1925, here in question, there is no issue as to income from personal services. Accordingly, nothing would be gained by an argument that the *earnings,* as distinguished from the investments of said earnings, were the separate property in equal proportions.

As shown by the findings [Tr. 32] these earnings were deposited in a joint bank account for petitioner and his wife and the investments in question were made with withdrawals from said account. Irrespective of the taxable status of the earnings, as such, the funds in the bank account and the investments therefrom had, under the express agreement of the parties, the status of separate property, owned equally by them as tenants in common.

Accordingly, in order to avoid confusion and to reduce the issues to a minimum, counsel for petitioner have conceded, for purposes of this appeal, that the earnings from personal services were taxable entirely to the hus-

band, under the principle laid down in *Lucas v. Earl*, 281 U. S. 111.

Obviously, there is no inconsistency involved in this concession, but merely an effort to protect the court from the consideration of unnecessary and irrelevant issues.

Respectfully submitted,

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